

# AREAS OF RECURRING TAXPAYER NONCOMPLIANCE

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## ■ Returns Processing Center

*Each year the Returns Processing Center of the Indiana Department of Revenue is responsible for processing nearly 6 million tax returns and the deposit of over 6 billion dollars. In our efforts to serve our customers who represent a vast cross section of interests we find a number of problems that continue to occur from one year to another. Our goal is to see that all returns are received, the remittances and the returns are posted to the accounts both timely and accurately, and for those taxpayers expecting a refund that those monies are paid timely and accurately. As with all businesses we are looking at various means of new technology to assist us in achieving our goals. But even with the use of new technology we still find the following areas of recurring taxpayer noncompliance.*

### Use of Non-Departmental Payment Coupons

The Department provides preprinted coupon vouchers to taxpayers who are registered with the Department and have a previous history of filing coupons. Relevant tax types include: sales tax, withholding tax, estimated tax for both individuals and corporations, and various other taxes and fees. Each month the Department receives several thousand payments without coupons, maybe with handwritten information on pieces of paper, coupons from prior filing periods that have been changed to fit the periods for which the taxpayers are trying to file, or just payments with no explanation. The Department receives numerous coupons generated by tax preparation software that cannot be processed by our automated equipment, which cause them to be manually processed.

### Failure to Complete All the Required Lines/Information

The Department receives numerous returns that are not completed by the taxpayer, which delays their processing and necessitates Department personnel having to complete the form based on the information provided, contacting the taxpayer, or returning the form to the taxpayer for additional information. These problems slow down the Department's ability to process returns quickly and efficiently.

## Filing the Wrong Return

The Department receives numerous returns each year which are on the correct forms but not for the current year, or may be for the correct year but are on the wrong forms. An example would be taxpayers' submitting IT-40EZ forms, when they do not qualify for that form because of the type of income or deductions they may have. In these cases, Department employees must determine the correct form to be used and either attempt to transfer the information to the correct form, or return the form submitted along with a copy of the correct form to the taxpayer for resubmitting.

## Failure to Attach W-2 Forms

The Department receives a vast number of Individual Income Tax returns without W-2 forms to verify the withholding taxes taken as credits on the returns. Failure to submit W-2 forms causes the returns to be rejected and returned to taxpayers with requests for correct documentation.

## Failure To Attach W-2 Forms with the WH-3

The W-3 is a reconciliation of the W-2 forms; and both the WH-3 and all W-2 forms must be submitted together annually. The Department often receives WH-3 forms without W-2 forms attached. It also often finds cases of taxpayers changing business names during the year but continuing to file their taxes under their previous Identification Number, and then using the incorrect forms at the end of the year to submit their withholding information for the year.

## Failure to Attach the Necessary Schedules

The Department finds that often taxpayers take credits on their tax returns, but fail to include documentation or necessary schedules to substantiate the deduction or credits being taken (e.g. College Credit, Form CC-40).

## Failure to Comply with Enterprise Zone Deduction

If a taxpayer lives in an Enterprise Zone and works for a qualified employer in that zone, the taxpayer may be qualified to take the deduction. The deduction is one-

half (1/2) of the earned income shown on form IT-40QEC, or \$7,500, whichever is less. Often the deduction is calculated incorrectly, or Form IT-40QEC, which should be provided and completed by the employer, is not attached to the taxpayer's Form IT-40.

### **Taxpayer Filing Wrong Form**

Taxpayers who are residents from Reciprocal States often file on Indiana Form IT-40 and take a deduction of the other state's income, rather than filing the appropriate Indiana Form IT-40RNR (Reciprocal Nonresident).

### **Penalty for Underpayment of Estimated Tax**

Taxpayers often owe penalties for underpayment of estimated taxes if they didn't have taxes withheld from their income and/or didn't pay sufficient estimated taxes throughout the year. Generally speaking, if a taxpayer owes \$400.00 or more in state and county taxes for the year that are not covered by withholding taxes, the taxpayer needs to make estimated tax payments.

### **Failure to Calculate County Tax**

Often taxpayers fail to compute their county taxes. If, on January 1 of the tax year, taxpayers lived and/or worked in an Indiana county that has a tax, they must figure their county tax. Failure to calculate county tax due may delay processing of their returns.

### **Improper Completion of County Boxes**

Some IT-40's are received with "00" in the county boxes when it is not applicable. An example is "00" entered in the spouse boxes for a single taxpayer. Our computer system recognizes "00" as meaning a non-reciprocal out of state county.

### **Systems Services Delinquency Project**

The Department issues delinquency letters to those Sales Tax and Withholding Tax accounts that fail to file returns for all periods. The taxpayer receives a letter indicating the tax type, delinquent month(s), quarter(s) or year along with the appropriate preprinted returns to be completed for those periods. This project is conducted to ensure compliance with the Department of Revenue's filing requirements and encourage proper notification of any changes that we may need to maintain accurate and current records.

### **Corporate Tax Failure To File Timely**

Corporate tax filings that show no tax liability, but are filed after the due date, are subject to a penalty of \$10

per day that the return is past due, up to a maximum of \$250. In years past, these billings were manually generated, but with the Departments Returns Processing System (RPS), the late returns are programmatically identified and the taxpayers subsequently billed.

### **Fuel Tax Common Reporting Errors**

A review of previously filed special fuel and gasoline monthly tax returns has revealed the following common reporting errors. This list does not contain all reporting errors, but is representative of those most commonly found. This would include the following forms and schedules: FT-1, SF701, MF360, Schedules 5 through 10, SF900, SF401, Schedules 1A, 2A, 3A, FT501, Schedule 501A, 501B, 501C, MF600, SF801 and SFIVP.

- Return submitted with no license/account number indicated
- Return submitted with no signature of person completing/filing return
- No payment submitted with a return that indicates an amount due
- Payment submitted but no return filed
- Missing schedules
- Incomplete information provided on schedules
- Transactions reported in the wrong month. (All special fuel transactions must be reported in the month in which they occur)
- Duplication of deductions on more than one schedule
- More than one fuel type reported on same schedule
- Export schedules not filed in duplicate as required
- Dyed fuel transactions reported on schedules designated as clear fuel
- Deliveries of special fuel with an Indiana destination misreported on export schedules
- Truck deliveries misreported on Schedule 6

- Computer generated forms/schedules that do not conform to Department requirements
- Dyed fuel user not filing schedule correctly

### Environmental Tax Common Reporting Errors

A review of previously filed environmental returns has revealed the following common reporting errors. This would include the following forms and schedules: UST-1, HC-500, HW-020 and SW-100.

- Form not signed
- No Federal I.D. number/social security number
- No check with form
- No form with check
- Check not made out to Indiana Department of Revenue
- Money sent is different from amount filled
- Missing schedules
- Duplicate filing

## ■ Compliance Division

### AERONAUTICS SECTION

The Aeronautics Section mailed 4,571 aircraft registration renewals for the Calendar Year 1999, 167 aircraft owners were delinquent. This translates to a 96% renewal compliance rate. The following amounts were collected and processed by the Aeronautics Section for the Fiscal Year 1999 – 2000.

Aircraft Sales/Use Tax	\$3,714,109
Aircraft Excise Tax	\$ 430,718
Registration Fees	\$ 79,612
Total	\$4,224,439

Indiana Code 6-6-6.5-2 states that any resident of this state who owns an aircraft must register the aircraft within thirty-one (31) days from the purchase date. Any non-resident who bases an aircraft in this state for more than

sixty (60) days shall register the aircraft with the Department no later than sixty (60) days after establishing a base in Indiana. During Fiscal Year 1999-2000, section actively pursued non-compliant aircraft owners that failed to respond to the Department's request for registration. Three hundred, sixty-eight (368) aircraft owners were assessed \$1,594,777. This amount includes delinquent prior year and current excise tax, sales/use tax, plus penalty and interest.

According to Indiana Code (6-6-6.5), airport owners who fail to report to the Department all based aircraft at their facility are subject to a late penalty of \$10.00 per day. Penalties totaling \$1,140 were collected from delinquent airports in Fiscal Year 2000. These reports are used to verify that all aircraft owners based in Indiana are in compliance with Indiana registration laws.

### Corporate Reinstatement Certificate of Clearance & Letters of Good Standing

Often profit and not-for-profit corporations allow their corporate status to be administratively dissolved by the Secretary of State's Office for noncompliance. The taxpayer is required to obtain a reinstatement certificate of clearance from the Department verifying the corporation is in good standing before their corporate status will be reinstated with the Secretary of State's Office. The Department has issued 911 reinstatement clearances, and denied 89 requests.

Corporations in the process of obtaining financial loans or grants will request the Department to issue a letter of good standing for their corporation. The Department has issued 106 letters of good standing and denied 31 request.

### BANKRUPTCY/RESPONSIBLE OFFICER SECTION

The Bankruptcy Section receives notification from federal district courts of bankruptcies related to the State of Indiana. The Department of Revenue is required to file proofs of claims with the courts of any outstanding Indiana tax liabilities. During the Fiscal Year 2000, this section filed 2,218 claims with the U.S. Bankruptcy Courts, totaling \$38,323,610 representing unpaid tax delinquencies and projected tax liabilities for non-filed returns.

A responsible officer is an individual who is an employee, officer, or member of a corporate or partnership and has the duty to remit trust taxes to the Department of Revenue. The responsible officer is personally liable under Indiana Code 6-2.5-9-3 and Indiana Code 6-3-4-8(g) for the payment of these taxes. Trust fund taxes are comprised predominantly of sales/use and withholding taxes.

During Fiscal Year 2000, responsible officers were assessed \$3,864,962 in delinquent trust taxes.

## **CHARITY GAMING/NOT-FOR-PROFIT**

This section is responsible for determining organizations' not-for-profit status and for licensing qualified not-for-profit organizations for bingo, festivals, raffles door prizes, and charity game nights. The licensing of manufacturers and distributors to sell tip boards, punch boards, and pull-tabs is performed by this section.

A total of \$4,061,892 in fees was collected from the following licenses issued:

<b>Type of License</b>	<b>Number of Licenses Issued</b>
Annual Bingo	895
Charity Game Night	255
Door Prize	8
Festival	294
Raffle	535
Special Bingo	133
Total License Issued	2,120

The following license fees were collected:

Gaming License Fees	\$ 3,907,892.00
Manufacturers License	\$ 36,000.00
Distributors License	\$ 118,000.00
Total Fees Collected	\$ 4,061,892.00

During the Fiscal Year 2000, the Charity Gaming Section conducted four training seminars, which were held in Indianapolis, Plymouth, Madison and Jasper. Approximately 252 representatives from not-for-profit organizations attended these seminars which covered the following topics:

- Not-For-Profit Tax Registration
- How to Qualify to Conduct Charity Gaming in Indiana
- Rules and Regulations
- Bookkeeping and its Importance
- Charity Gaming Excise Tax – rules and procedures
- Common errors that may delay processing
- Penalties and Fines imposed for gaming violations

## **Charity Gaming**

The Department will be sponsoring six training seminars around the state during the next fiscal year. These seminars will be held in Indianapolis, Plymouth, Huntington, Marshall, Mitchell, and Madison. The seminars will help explain the laws and regulations for not-for-profit organizations which either currently conduct, or would like to conduct, charity gaming activities. The topics will cover the qualification process, forms, financial reports, as well as changes to forms and procedures.

## **INDIVIDUAL/WITHHOLDING SECTION**

The Individual Income Tax Section's mission is to identify and pursue non-filers; as well as to verify the accuracy of filed returns, utilizing information from the Internal Revenue Service, various Indiana State agencies, other state taxing agencies, and anonymous informants. Our standard compliance projects and findings for Fiscal Year 2000 are as follows:

### **Federal Audits**

The Internal Revenue Service provides agreed federal tax audit reports to the Department. If taxpayers fail to amend their Indiana Individual Income Tax return to report the Indiana adjustments resulting from the federal modifications, a tax assessment is generated. This project resulted in 2,221 taxpayers being assessed a total of \$1,787,427.

### **CP2000**

The Department receives data from the Internal Revenue Service regarding taxpayers who failed to report all taxable income. This could be income derived from wages, interest, dividends, or non-employee compensation. These types of income are reported on W-2's or Form 1099 information statements. An assessment is generated if the income was not reported on the original return, or an amended return. The project resulted in 12,466 taxpayer assessments totaling \$1,788,678.

### **Individual Desk Audits**

Individual desk examinations are performed, based on anonymous sources or submissions from other divisions within the Department. The examination may consist of verifying income reported, credits/deductions taken, or the amount of refund requested. The Section assessed 116 taxpayers \$78,544 through these audit efforts.

## **Withholding Discrepancies**

A comparison is made between taxpayers' annual WH-3 Forms with the state and county withholding payments (WH-1) made during the year. If underpayments exist, taxpayers are assessed the differences. The project resulted in 1,699 taxpayers being assessed \$6,986,000.

## **STRATEGIC SECTION**

The Strategic Section of Compliance was created to research, develop, and implement projects designed to increase taxpayer education and voluntary compliance. As needed, we also assist other sections of the Department to eliminate processing backlogs. This section may be assigned to answer telephones, work correspondence, examine returns and filing information, or work on tasks that assist in meeting Departmental goals.

As the Department added Corporate Income Tax data to our on-line computer system, this section helped eliminate backlogs. This section reviewed 9,373 corporate income tax returns and collected \$10,660 while pursuing this endeavor.

Educational efforts continued to inform professional and service-oriented businesses that they might have a use tax liability. Use tax is due when a purchase is made and there was no sales tax imposed. This would include purchases made from suppliers or vendors outside Indiana. Examples of such purchases subject to use tax would include, but are not limited to professional books or publications, computer hardware or software, office equipment, and magazine subscriptions. Letters providing information on use tax requirements were sent to 3,752 taxpayers, which resulted in the collection of \$93,965.

This section contacted 607 taxpayers who were delinquent in multiple tax areas. These taxpayers were contacted by telephone or mail and informed of missing tax returns before any assessments were issued. This project resulted in taxpayers filing returns for the appropriate tax periods and remitting taxes totalling \$239,258.

Much research was conducted this year on referrals received from other divisions of the Department, other state agencies, as well as revenue agencies from other states. As a result of taxpayer correspondence and assessment notifications, the Section collected \$1,798,266.

Departmental records were examined to identify non-filers of individual income tax, sales/use tax, withholding tax and corporate income tax. Taxpayers were sent letters to educate them on filing requirements, as well as penalty and interest assessed if they fail to timely file and remit tax due. Total collection for the fiscal year was \$141,640.

## **UTILITY/REFUND SECTION**

Sales and use tax imposed when property is acquired from a retail merchant in a retail transaction. Since Indiana Code 6-2.5-4-5 excludes utility sales for listed uses from being retail transactions, that cannot be subject to sales or use tax. This exclusion applies when the sales of the utility are (1) by public utilities power subsidiaries, or person engaged as public utility (2) used in manufacturing, production, etc. and (3) either separately metered or predominately used in an excluded manner.

To receive this exclusion, the taxpayer must complete Form ST-200, Utility Sales Tax Exemption Application. The application is utilized by the Department to determine if a taxpayer qualifies for a full or partial exemption. This section reviewed and processed 5,381 Utility Sales Tax Exemption Applications.

Approximately 3,059 refund claims (Form GA-110L) were processed and approved totaling \$40,660,143. Original amounts claimed were reduced by \$700,631. As a result of taxpayer failure to document the claims, failure to meet exemption requirements and/or the Statute of Limitations had expired. In addition, \$35,762,424 (of the amount claimed) was assigned to other divisions for review.

## **Voluntary Compliance Agreements**

Taxpayers who have failed to collect/remit taxes occasionally contact the department and request to enter into a Voluntary Compliance Agreement. These taxpayers may have been unaware of State filing requirements or may have failed to file tax returns. Collections for Fiscal Year 2000 totaled \$293,423.

## **Collections**

Consumer use collections, payments received from out-of-state companies (who either collected Indiana Sales Tax or owed Indiana Use Tax) and billings generated from information received from a variety of sources, i.e. other state agencies, divisions, states, anonymous tips, etc., resulted in the collection of \$397,267.

## **Fuel and Environmental Refund**

The Trust Refund Section was expanded to include some employees of the former Fuel and Environmental Division. These employees are responsible for reviewing Gasoline (Form GR-4136), Special Tax (Form SFR-1032) and Proportional Use (Form MF-6431) refunds. The Prepaid Sales Tax staff has joined this section, as well; their primary responsibilities include the review and maintenance of the Prepaid Sales Tax accounts.